

## **AS WE APPROACH OUR DIAMOND ANNIVERSARY: A VISION FOR BPA**

**Restoring luster to the Northwest's crown jewel:  
The Federal Columbia River Power System**

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If you want to know the mantra around the Bonneville Power Administration these days, it's this – reliability, environmental stewardship, low rates consistent with sound business principles, and regional accountability.

These four are the historic core values of this agency, and we intend them to define our future as well. In fact, it is our vision that the Northwest is a leader in these areas long into the future.

We have always stood for these values, but in recent years they seem to have been somewhat lost in the shuffle as we've been buffeted by so many near-term changes, starting with wholesale power deregulation in the early '90s and more recently the West Coast energy crisis and Northwest drought in the winter of 2000-2001. We are still feeling the reverberations of those overlapping events, and our near-term focus has been to recover from the financial hole they put us in.

While we are not out of the woods and still have quite a way to go, we have made progress. We believe now is the time to renew our focus on the longer term. This means addressing three important realities. First, the Federal Columbia River Power System still provides enormous value to the region. Second, the value of the system is finite and, with a number of costs loaded onto the system, its true value has become clouded. And, third, we must take steps to preserve the inherent value of this tremendous resource now and into the future. That's what I want to talk to you about today.

In 2012, we will celebrate the diamond anniversary of BPA. On that anniversary, I want a BPA Administrator to be able to stand before you and say these things.

- We are among the most reliable electricity systems in the country.
- Our wholesale rates are well below the market for comparable long-term products.
- Our efforts to preserve the environment of this great region have paid off.

- And we have been accountable to the people of the Northwest and have earned their trust.

This is my vision. If we can do that, we will have restored the luster of the region's crown jewel — the Federal Columbia River Power System.

Here are eight challenges that make a compelling case for taking action. I believe they are the critical factors that we need to address.

### **Critical factors driving strategy:**

1. The recent 50 percent increase in BPA power rates has seriously eroded customer trust and confidence, and it could pose a threat to the agency's competitiveness if rates were to continue to rise. In addition, BPA is exposed to greater and increasingly complex risks.
2. While salmon returns have been improving, escalating costs for fish and wildlife have increased the need to adopt clearly defined objectives and to determine the most cost-effective means of achieving success.
3. The true value of the very low-cost federal hydro system has been masked by additional costs that have been melded with the low-cost hydro.
4. BPA's financial health has suffered as a result of the West Coast energy crisis and Northwest drought of 2000-2001. While our financial position has improved, we must restore and sustain our financial health to ensure that we meet our responsibilities to both ratepayers and taxpayers.
5. The region's infrastructure requires investments in generation, conservation and transmission if it is to maintain reliability and adequacy and provide the necessary foundation to support a healthy economy.
6. The absence of a regional approach in conservation, generation acquisition, and transmission planning and expansion has hampered regional investment in infrastructure.
7. Customers, tribes and constituents have criticized BPA for the complexity of its ratemaking processes and for its lack of clarity in financial reporting and decision making.
8. Faced with the need to cut costs, BPA has substantially reduced investments in innovative technologies and has made deep cuts in investments in its people.

### **Meeting the challenges ahead**

Together, these eight factors clearly dictate a need for change — and not just in the short term. So what are we planning to do about it? We at BPA have renewed our

focus on the long term and have developed a strategic plan to achieve the vision that will make us a leader in reliability, low cost power and transmission services consistent with sound business principles, environmental responsibility and accountability to you, the citizens of this region.

As we developed the strategic plan, we assumed that our goals would be accomplished without new legislation. We also remained committed to three fundamentals of our existing statutory mission, which include cost-based rates, public preference and regional preference in the marketing of power. One notable change is that we have rewritten our mission statement to elevate fish and wildlife mitigation to one of three fundamentals of our mission, along with marketing power and providing transmission.

We are sharing this plan with you and others in the region through a number of public processes. This plan is not a decision document, nor is it a “tell.” We are sharing our ideas, and we want to know what you think about them. We are very interested in your comments.

Here are the areas our vision addresses.

## **1. Lowering rates**

First, clearly we need to address rates. After years of real and nominal declines in our power rates, BPA rates increased by 50 percent between 2001 and 2003. While the agency’s competitive position relative to comparable products – particularly long-term supply options – remains strong, managing rates has become a critical issue from several standpoints. These include the impacts on the regional economy, competitive challenges that BPA could face and customer confidence. Our goal is for power rates to go down in 2007 and transmission rates to be kept to a modest increase, all while remaining fiscally prudent. As transmission rates are only about 10 percent of power rates, total rates of delivered power should decrease for the region’s ratepayers while BPA retains the ability to fully meet its obligations to the nation’s taxpayers.

We also know that BPA has to develop a robust risk management system if we are to minimize rate volatility. Few businesses face the level of risk that BPA experiences. Ninety percent of our power is hydro, which depends on the weather. And, on average, around a quarter of our revenues come from selling variable amounts of hydro into secondary electricity markets. Clearly, risk management is critical to our success.

Most important, we need to make sustained cost management a way of life, and we need to be great operators of the core system. We have been made stewards of the hydropower and transmission assets of this hugely valuable system, and, along with our partners – the U.S. Corps of Engineers, Bureau of Reclamation and Energy Northwest – we must seek continuous improvement and efficiencies in how we operate these assets.

## **2. Setting objectives for fish and wildlife mitigation and managing to them cost effectively**

Second, we need to protect fish and wildlife, but efficiently. Improved survival of salmon within the federal hydro system suggests that our investments are creating value. We have seen tremendous increases in the number of returning adult fish in the past three years. While we know improved ocean conditions played a great part in that, we believe that ratepayer efforts have also substantially contributed because we are also seeing improvements in juvenile fish survival.

We want to keep the momentum but do so efficiently. The program needs clearly defined performance goals. Fish and wildlife costs have increased from \$150 million annually to over \$600 million annually. Because there is so much at stake, we need to focus all our programs on performance, and we need to be alert for opportunities to deliver comparable or greater benefits at lower cost. Without specific goals, it is difficult to evaluate the most cost-effective paths to achieving success. This is critical because program costs cannot continue to escalate without substantial rate increases, and Northwest citizens will not support a program they perceive is inefficient.

This is not a smoke screen to do less for fish but rather an urgent call to make sure that success of the program is based on performance. Let me state unreservedly that we believe in the importance of our region's fish and wildlife and their environment. As I said earlier, we have elevated fish and wildlife mitigation to become part of our new mission statement. We intend to leave as light a footprint on the environment as possible. Congress and the people of the Northwest expect nothing less.

## **3. Preserving the value of the federal base system**

Third, we must preserve the considerable value of the federal base system that BPA manages. Although this value is derived fundamentally from the federal hydro system, we have not built new dams for 30 years, and we're not going to be building more. We can only increase the value of this system by finding more efficiencies in our operations and new ways to use the system to support the region. Our rates have risen as we have been adding costs to the system more quickly than we have been adding efficiencies. As costs have increased and rates have risen, the value of the system has become unclear to the region's citizens.

A review of our cost structure showed that the single biggest driver of the recent power rate increases was the increase in load served by BPA. Clarifying who has the obligation to serve load is one of the most important issues we need to resolve. BPA must address and define the amount of load we will serve at a melded rate, and we will actively explore tiered rates as a way to keep costs down. We envision that tier 1 would be rates for the low-cost federal resources, while tier 2 rates would cover acquiring higher-cost resources. Tiered rates would help assure that our core public preference customers continue to realize the benefits of the federal system into the future.

#### **4. Protecting taxpayers and ratepayers**

Fourth, BPA must meet its responsibilities to taxpayers and ratepayers, and it can do that best by ensuring its financial health. The federal taxpayer has made a significant investment in the Northwest hydro system. BPA is responsible for repaying these costs on time and in full. If BPA is not a good financial steward and is deficient in making its annual repayments to the U.S. Treasury, we put at risk our ability to retain the benefits of the system.

Rates must be set to fully recover BPA's costs. Cash and revenue positions must be consistently positive, and BPA must have sufficient financial reserves to maintain a high probability of making our annual payment to Treasury. Good financial stewardship has additional benefits for ratepayers. Higher credit ratings mean lower interest and transaction costs, and that translates to lower rates.

Properly structured, long-term contracts could also provide further stability and predictability for taxpayers and ratepayers. Such contracts would assure that Northwest ratepayers get continued access to the low-cost federal system at cost-based rates and that taxpayers are repaid for their investment.

#### **5. Building our share of the region's infrastructure**

Fifth, BPA must invest in infrastructure to assure the reliability and adequacy of the region's electrical system. Investments in generation, conservation and transmission are clearly needed to support a growing economy, ensure reliability and minimize future price volatility. BPA will invest in infrastructure on its own system and will capture all cost-effective conservation within its own load. I reaffirm our view that the best way to maximize the value of our inexpensive hydropower base is to use it efficiently in Northwest homes, farms and businesses. The longstanding BPA electricity mandate of "widest possible use" cannot be achieved today without doing all we can to promote "wisest possible use."

We will sustain our industrywide leadership in creating a full portfolio of solutions to transmission congestion and reliability problems, including but not limited to demand-side investments, sophisticated new technology for getting more work out of fewer wires, and constructing additions to our network where needed.

With Administration support, Congress authorized an increase in BPA's ability to borrow money from the U.S. Treasury, but we may not be able to count on further timely increases. BPA must develop a long-term capital plan that assures adequate access to capital for cost-effective investments in infrastructure.

## **6. Supporting regional approaches to regional infrastructure development**

With deregulation, our electricity infrastructure has become highly complex and, in some cases, more fragile. BPA cannot support the entire regional infrastructure, and the region needs to take an integrated approach in key areas such as conservation and renewable resource acquisition, reliability and adequacy standards, and transmission. The Northwest Power and Conservation Council is uniquely qualified to define goals for the region's future power supply including the development of conservation and renewable resources. We look forward to continued energy efficiency partnerships with our utility colleagues across the region, starting with and building on our remarkably successful Northwest Energy Efficiency Alliance. We will also provide products and services to facilitate development of both conservation and generation, including renewable resources, by others.

We likely also will need new institutions to address an integrated regional approach to transmission planning, expansion and operation. Electricity flows across the path of least resistance and ignores the vagaries of ownership structures. An approach that plans and operates the system as if it were run by a single utility will best serve consumers. Moving to consolidate regional transmission operations would also enhance the operational excellence necessary for reliability. And our broadly based Roundtable on Non-Wires Solutions already is helping the entire region develop new options for improving transmission performance at lower economic and environmental cost.

## **7. Seeking simplicity and transparency**

Seventh, we need to make our systems and processes simpler and more transparent if we are to have a collaborative relationship with our customers and Northwest citizens. Recent rate increases have generated broad and vocal customer dissatisfaction with BPA. We have heard the concerns that BPA's decision making processes are perceived as overly complex and unclear.

Much of the complexity has been added to the system because of increasing demands to share in the benefits of a system that is not growing. Consequently, the effort to provide precise equity has produced elaborate contractual provisions and formulas. Not only do these solutions add complexity, but they also add substantial administrative costs. We know we must simplify our processes and seek greater transparency in our decision making and financial reporting.

## **8. Investing in the future**

Eighth, we need to invest in our future capability. BPA has a proud history of helping create and apply technologies critical to our own business challenges and to the industry's development. Such investment creates opportunities for a better future through lower costs and better environmental protection. Currently, the electric power industry is investing very little in technological innovation. Yet there are promising developments, and the potential for applying technological gains from other industries could ultimately

improve performance and create efficiencies for our region's electricity industry. We have a unique opportunity in the Northwest thanks to budding industries that are developing new digital technologies that have applications to the electric power industry. We want to be a center of innovation also for the transmission, hydroelectric, energy efficiency, and renewable energy technologies that are so crucial to the region's long-term competitive success.

We also need to invest in our people. BPA has dramatically cut areas such as training and performance rewards for staff. These were necessary actions given our rates and financial situation. But these actions are not effective as a long-term strategy. The region has a lot at stake. BPA performs a critically important function for the region, something we all think of quite literally as "keeping the lights on." It takes great skill to run a world-class electricity system, and it's essential that we attract and retain the best, the brightest and the most dedicated employees to our organization.

### **In conclusion**

To close, let me underscore that the federal hydropower system has been a source of economic strength for this region for nearly 70 years. We at BPA and the region as a whole need to take actions to assure it continues to provide this value well into the future. Those actions, I believe, fall in the eight broad categories I have described. To quickly reiterate, they include:

1. Lowering rates consistent with sound business principles;
2. Setting objectives for fish and wildlife programs and managing to them cost effectively;
3. Preserving the value of the federal base system;
4. Protecting taxpayers and ratepayers;
5. Building our share of the region's infrastructure;
6. Supporting regional approaches to regional infrastructure development;
7. Seeking simplicity and transparency; and
8. Building for the future.

I began this discussion by naming the four core values that should define BPA: reliability, environmental stewardship, low-cost power and transmission services consistent with sound business principles and regional accountability. I believe if we are successful in the eight areas I have outlined, we will live up to our vision statement, which calls on BPA to advance the Northwest's national leadership in these four values by meeting our public responsibilities through a commercially successful business.

The world may be far more complicated than it was when BPA was created in 1937, but I believe that our focus remains simple and clear. The Federal Columbia River Power System is the crown jewel among the Northwest's resources. It is our job to preserve and polish it. I want it to shine long before our diamond anniversary, which is less than a decade away. We can do that by being excellent –not just good –operators of this great system.

